



April 1991

# Office of the Legislative Auditor

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State of Montana

Report to the Legislature

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## Financial-Compliance Audit

For the Two Fiscal Years Ended June 30, 1990

### State Auditor's Office

This report contains ten recommendations for improvement of the office's operations. Major issues addressed in the report include:

- ▶ Compliance with appropriation laws to prevent the overspending of appropriations.
- ▶ Compliance with state laws regarding valid obligations which results in \$24,780 due to the General Fund.
- ▶ The annual licensing of nonresident insurance producers which could generate an additional \$41,850 for the General Fund.

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## **FINANCIAL-COMPLIANCE AUDITS**

Financial-compliance audits are conducted by the Office of the Legislative Auditor to determine if an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations which could have a significant financial impact. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States General Accounting Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

The Single Audit Act of 1984 and OMB Circular A-128 require the auditor to issue certain financial, internal control, and compliance reports regarding the state's federal financial assistance programs, including all findings of noncompliance and questioned costs. This individual agency audit report is not intended to comply with the Single Audit Act of 1984 or OMB Circular A-128 and is therefore not intended for distribution to federal grantor agencies. The Office of the Legislative Auditor issues a statewide biennial Single Audit Report which complies with the reporting requirements listed above. The Single Audit Report for the two fiscal years ended June 30, 1989 has been issued. Copies of the Single Audit Report can be obtained by contacting:

Office of the Legislative Auditor  
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Helena, MT 59620

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April 1991

The Legislative Audit Committee  
of the Montana State Legislature:

This is our financial-compliance audit report on the State Auditor's Office financial activity for fiscal years 1988-89 and 1989-90. Issues discussed in this report include compliance with appropriation laws to prevent overspending appropriations and compliance with state laws. The office's written response to the audit recommendations is included in the back of the audit report.

We thank the State Auditor and her staff for their cooperation and assistance throughout the audit.

Respectfully submitted,

  
Scott A. Seacat  
Legislative Auditor

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# **Office of the Legislative Auditor**

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**Financial-Compliance Audit**

**For the Two Fiscal Years Ended June 30, 1990**

## **State Auditor's Office**

Members of the audit staff involved in this audit were: Donna Aschenbrener, Laurie Evans, John Fine, Wayne Kedish, Maureen G. McHugh, and Charles Nemec.



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## **Elected and Administrative Officials**

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### **State Auditor's Office**

Andrea "Andy" Bennett, State Auditor

J. Dennis Sheehy, Deputy State Auditor

David Barnhill, Deputy  
Insurance Department

Robyn Young, Deputy  
Securities Department

Debbie VanVliet, Administrator  
Fiscal Control/Management Division

Donna Warner, Deputy Director  
State Payroll Division



## Summary of Recommendations

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The listing below serves as a means of summarizing the recommendations contained in the report, the State Auditor's Office response thereto, and a reference to the supporting comments.

<u>Recommendation #1</u>	We recommend the State Auditor's Office comply with the provisions of its appropriation laws. ....	5
	<u>Agency Response:</u> Concur. See page 31.	
<u>Recommendation #2</u>	We recommend the State Auditor's Office comply with the personal service restrictions in the appropriation law. ....	6
	<u>Agency Response:</u> Partially Concur. See page 31.	
<u>Recommendation #3</u>	We recommend the State Auditor's Office:  A. Accrue only valid obligations as defined by state law.  <u>Agency Response:</u> Concur. See page 31.  B. Revert \$24,780 of appropriation authority to the General Fund. ....	7
	<u>Agency Response:</u> Do Not Concur. See page 31.	
<u>Recommendation #4</u>	We recommend the State Auditor's Office record revenue in the General Fund for money received from the sale of copies and documents. ....	8
	<u>Agency Response:</u> Concur. See page 32.	
<u>Recommendation #5</u>	We recommend the State Auditor's Office:  A. Establish procedures to ensure the accuracy of payments to the Public Employees' Retirement Division prior to making payments.  <u>Agency Response:</u> Concur. See page 32.	

## Summary of Recommendations

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- B. Work with the Public Employees' Retirement Division to determine the amount of money owed for late pension payments.. . . . . 10

Agency Response: Concur. See page 32.

### Recommendation #6

We recommend the State Auditor's Office:

- A. Record all expenditures and revenue related to examinations of domestic insurance companies on the state's accounting records in accordance with state law.

Agency Response: Do Not Concur. See page 33.

- B. Charge insurance companies for the time spent conducting examinations in accordance with section 33-1-413, MCA.

Agency Response: Do Not Concur. See page 33.

### Recommendation #7

We recommend the State Auditor's Office prepare written contracts for contracted services prior to the commencement of work. . . . . 13

Agency Response: Concur. See page 34.

### Recommendation #8

We recommend the State Auditor's Office:

- A. Charge the fees for insurance producers as required by state law.

Agency Response: Concur. See page 34.

- B. Seek legislation clarifying inconsistent licensing laws. . . . . 15

Agency Response: Concur. See page 34.

### Recommendation #9

We recommend the State Auditor's Office transfer \$71,038 remaining cash balance in the Firemen's Pension Special Revenue account to the new pension account as required by state law. . . . . 16

Agency Response: Do Not Concur. See page 34.

## Summary of Recommendations

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### Recommendation #10

We recommend the State Auditor's Office notify the state Department of Revenue of abandoned property held by Montana insurance companies in accordance with state law. . . . . 16

Agency Response: Concur. See page 35.



# Introduction

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## General

We performed a financial-compliance audit of the State Auditor's Office (office) for fiscal years 1988-89 and 1989-90. The objectives of our audit were to:

1. Determine if the office complied with applicable laws and regulations.
2. Make recommendations for the improvement in administrative and accounting controls of the office.
3. Determine if the office's financial schedules present fairly the results of operations for the two fiscal years ended June 30, 1990.
4. Determine the implementation status of prior audit recommendations.

This report contains ten recommendations to the office. Other areas of concern deemed not to have a significant impact on the successful operations of the programs within the office of the State Auditor are not specifically included in the report, but have been discussed with management.

In accordance with section 5-13-307, MCA, we analyzed and disclosed the cost, if significant, of implementing the recommendations.

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## Office Background and Organization

Article VI of the Montana Constitution establishes the State Auditor's Office. The State Auditor is an elected position with a term of four years. Responsibilities of the State Auditor's Office include the following: superintending the fiscal duties of the state, suggesting plans for improvement and management of public revenues, keeping an account of all state warrants, and collecting and paying into the state treasury all fees it receives.

The State Auditor is both the Commissioner of Insurance and Commissioner of Securities. Insurance duties relate to licensing and regulating insurance companies within the state. Securities duties relate to regulating security transactions in the state. The

## Introduction

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State Auditor is also director of the state's central payroll system and administers the bad debt collection function for the state. The office is divided as follows:

1. Central Administration is responsible for the administrative, budgeting, personnel, and accounting functions of the office. Legal services and word processing are also included in this division.
2. State Payroll prepares payroll for state agencies. The payroll system produces bi-weekly payroll checks; withholds and deposits all elective and mandatory deductions from employees' checks; and files required state and federal tax, unemployment and workers' compensation reports. The division is also responsible for maintaining the data base for the state Payroll/Personnel/Position Control system.
3. The Insurance Department regulates the insurance industry in Montana. Duties include: resolving insurance consumer inquiries and complaints involving agents, coverage, and companies; licensing and reviewing the market and financial condition of insurance companies; collecting insurance premium tax; reviewing all rates and forms used by insurance companies; licensing and testing all agents seeking to conduct insurance business in the state; and investigating insurance code and rule violations.
4. The Securities Department is responsible for the administration and enforcement of the Securities Act of Montana. The department is responsible for the registration of securities issuers, salesmen, investment advisers, broker-dealers, and investment adviser representatives. Additionally, it investigates instances of unregistered or fraudulent securities transactions.
5. Fiscal Control and Management is responsible for issuing state warrants and collecting bad debts. The division processes and records all state warrants including duplicate, emergency, cancelled, and stale-dated warrants. The bad debt function collects debts owed to the state.

The office is responsible for distributing a portion of insurance premium taxes to the Montana Public Employees' Retirement Division and to fire and police departments in qualifying Montana cities and towns. The office also distributes federal forest reserve moneys to Montana counties.



# Prior Audit Recommendations

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## **Prior Audit Recommendations**

The financial-compliance audit report of the State Auditor's Office for the two fiscal years ended June 30, 1988 contained ten audit recommendations. We determined the office implemented all ten recommendations.

# Findings and Recommendations

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## **Compliance with Appropriation Laws**

As part of our audit of the office, we tested compliance with the state's appropriation laws. This testing included reviewing compliance with restrictions contained in appropriation laws and reviewing appropriations each fiscal year to determine if transfers of spending authority were proper. The following report sections discuss concerns noted during our audit.

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## **Transferring Expenditures to Avoid a Negative Appropriation**

House Bill 2, Laws of 1987, appropriated \$112,442 in fiscal year 1988-89 for additional insurance regulation personnel. This line-item appropriation was to be used to pay personnel service costs associated with hiring an actuary, a field investigator, and an administrative aid in the Insurance Department. During fiscal year 1988-89, the office filled the field investigator position for the entire year and the administrative aid position for less than three months. The actuary position was not filled. We found the office charged \$37,450 to the additional insurance staff appropriation for nonpersonal services expenditures. Some examples of the inappropriate charges are:

1. Purchase of room dividers costing \$9,948 for the word processing area at the State Auditor's Office.
2. Charges for travel expenses of \$2,500.
3. Postage charges of \$23,500 transferred from the insurance regulatory appropriation.

Office personnel indicated these expenditures were transferred to the additional insurance staff appropriation because the office had exceeded the operating appropriation for the Insurance Department. If the charges had remained in the regular Insurance Department appropriation, the appropriation would have been overspent by \$36,549. Section 17-8-103, MCA, states it is unlawful for an agency to have expenditures in excess of appropriations. This law also states that a condition or limitation contained in an appropriation act shall govern the administration and expenditures of the appropriation. The State Auditor's Office should have complied with the language in House Bill 2,

## Findings and Recommendations

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Laws of 1987, and only charged personal service expenditures to the line-item appropriation for additional insurance staff.

### Recommendation #1

We recommend the State Auditor's Office comply with the provisions of its appropriation laws.

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#### **Transferring Personal Services Expenditures Between Programs**

The State Auditor's Office transferred personal service expenditures between programs during fiscal year 1989-90. We noted instances where the office partially charged the salaries of six employees to programs other than the program budgeted. House Bill 100, Laws of 1989, prohibits the transfer of personal services between programs. In addition, section 33-1-301, MCA, states that funds appropriated for the Insurance Department shall be used solely for the purposes for which they were appropriated. The following table shows where the amounts would have been charged if the employees' salary had been paid in the program where they worked.

#### Personal Service Transfers

<u>Program</u>	<u>(Over)/Under Expenditures</u>
Central Administration	\$ 6,430
Fiscal Management and Control	2,612
Securities	(176)
Insurance	(8,866)

Source: Compiled by the Legislative Auditor's Office

The Central Administration and the Fiscal Management and Control program expenditures would have exceeded appropriations by \$3,368 and \$2,260, respectively, if the charges had remained in the budgeted program. Office personnel indicated payroll for employees is sometimes charged to other programs when they perform duties for other programs. We reviewed

## Findings and Recommendations

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employee time sheets and did not find any evidence of the employees working for other programs. We also talked to some of the employees or their supervisor and found no evidence they worked outside their normal duties.

Office personnel also said certain jobs budgeted in the Central Administration and the Fiscal Management and Control programs actually perform duties for the entire office, including the Insurance and Securities Departments. They believe this gives them the flexibility to charge part of certain employees' salaries to other programs. If office personnel believe certain jobs are of central benefit to the entire office, they should allocate a portion of the salaries for the positions to all the programs as part of the budget process. The amount allocated and charged should be supported by an allocation formula determined before costs are charged.

### **Recommendation #2**

**We recommend the State Auditor's Office comply with the personal service restrictions in the appropriation law.**

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### **Expenditure Accrual Made to Obligate the Balance of an Appropriation**

At fiscal year-end 1989-90, the office established a \$24,780 expenditure accrual for future computer systems development to be performed by the Information Services Division, Department of Administration (ISD). Section 17-7-302, MCA, allows agencies to obligate funds at the end of a fiscal year for computer system development if a valid written service agreement exists. The office submitted a work order for the project but did not complete a written interagency service agreement with ISD until August 20, 1990, almost two months after the end of the fiscal year. Since the law specifically requires a written interagency service agreement by the end of the fiscal year to support accrual of system development costs, the accrual is not valid. As a result, General Fund expenditures are overstated by \$24,780 in fiscal year 1989-90. The State Auditor's Office

## Findings and Recommendations

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should revert \$24,780 of appropriation authority to the General Fund.

### Recommendation #3

We recommend the State Auditor's Office:

- A. Accrue only valid obligations as defined by state law.
- B. Revert \$24,780 of appropriation authority to the General Fund.

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### **Reducing Budgeted Expenditures Rather Than Recording Revenue**

The State Auditor's Office abates budgeted expenditures when it receives money for making copies of documents for outside parties. Section 33-2-708, MCA, allows the office to charge \$.50 per page for each copy of documents on file in the office. This fee should be recorded as revenue in the General Fund when money is received for making copies. In addition, the office charges up to \$6 for a copy of the annual "Admitted Montana Insurance Carriers" book and abates printing services expenditures rather than recording revenue. We found instances of expenditure abatements on at least thirty transactions during fiscal year 1989-90. By abating budgeted expenditures, the office increases available appropriation authority. In effect, the abatements allow the office to use the same spending authority twice.

In order to reduce the possibility of an agency exceeding its expenditure authority, state policy (MOM 2-1230.30) allows expenditure abatements to be used only for corrections of amounts erroneously expended from an appropriation. Office personnel believe abating expenditures for copy machine charges is proper because they would not have the expenses associated with making the copies if none were requested. Office management said copy charges have been recorded as abatements for many years. Since state law includes a fee for copies, we

## **Findings and Recommendations**

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believe making copies is a cost of operating the office and the money received should be recorded as revenue to the General Fund. The office should develop a budget plan which properly reflects costs and revenue associated with copies of documents. The cost of printing the "Admitted Montana Insurance Carriers" book is a cost built into the office's budget and any money received for the book should be recorded as revenue.

### **Recommendation #4**

**We recommend the State Auditor's Office record revenue in the General Fund for money received from the sale of copies and documents.**

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### **Pension Payments**

The state contributes to the police and firefighter's retirement systems. State statutes provide for various supplemental and reserve fund contributions. The money used to make the state contribution payments comes from a tax on insurance premiums collected by the State Auditor's Office. Any tax collections not needed for the pension payments goes to the General Fund. Each year the Public Employees' Retirement Division (PERD) calculates the amount of money the State Auditor's Office needs to remit to PERD for the state's contribution to the police and firefighter's retirement systems. PERD requests the payments by letter, supported by documents, detailing the calculation of the payment. The payment requests contained errors which caused the office to overpay PERD by \$156,717 and \$154,893 for fiscal years 1988-89 and 1989-90, respectively. If the State Auditor's Office had checked the mathematical accuracy of the calculations, office personnel would have discovered errors in the calculation of the police officer's supplemental payment for both fiscal years.

In addition to the overpayments, we noted the State Auditor's Office was late in paying the police and firefighter's pension contributions during fiscal year 1989-90. The payment due by

## Findings and Recommendations

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September 1, 1989 was not paid until October 31, 1989. State law requires the payments be made by the State Auditor's Office no later than September 1 each year. The total amount owed to PERD on September 1, 1989 was \$4,913,956. We estimated PERD could have earned \$67,610 in interest if it had received the payments on time. Office personnel stated controls ensuring timely payment were implemented subsequent to the 1989 payments. We noted the pension payments due by September 1, 1990 were made in advance of the due date.

The total effect on the General Fund caused by the overpayments and late payments is shown in the table below:

### Net Overpayments to PERD

	<u>Amount</u>
Fiscal Year 1988-89 Overpayment	\$156,717
Fiscal Year 1989-90 Overpayment	154,894
Lost Interest to General Fund Due to Overpayments	24,711
Pension System Lost Interest Due to Late Payments	(67,610)
Total	<u>\$268,712</u>

Source: Compiled by the Legislative Auditor's Office

After we notified the office of the overpayments, office personnel requested reimbursement from PERD for the overpayments and lost interest to the General Fund due to overpayments. The request was not adjusted for the interest the pension systems lost because of the late payments. PERD repaid the State Auditor's Office for the overpayments and interest. The office should work with PERD to determine what amount should be returned to PERD for the interest the pension systems lost because of the fiscal year 1989-90 late payment.

## Findings and Recommendations

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### Recommendation #5

We recommend the State Auditor's Office:

- A. Establish procedures to ensure the accuracy of payments to the Public Employees' Retirement Division prior to making payments.
- B. Work with the Public Employees' Retirement Division to determine the amount of money owed for late pension payments.

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### **Compliance and Clarification of State Laws**

We reviewed state laws and regulations pertaining to the office. The following report sections discuss compliance issues noted during the audit.

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### **Insurance Examinations**

Section 33-1-401, MCA, requires the State Auditor's Office Insurance Department to conduct an examination of domestic insurance companies at least every three years. A domestic insurance company is an insurer incorporated under the laws of the state of Montana. The following report sections relate to insurance examinations.

### **Examination Expense Not Recorded on the State's Accounting Records**

The Insurance Department performs insurance examinations or the office hires contract examiners to perform the work. Contract examiners are paid directly by the insurance company being examined. Payment is made for travel, living expenses, and the examiners' time. Contract examiners are paid at rates consistent with those published by the National Association of Insurance Companies (NAIC). State examiners are also paid directly by the insurance company for meals and lodging at state per diem rates when travel is required. Because the examiners are paid directly by the insurance companies, the activity is not recorded on the state's accounting records. During the audit period, there were approximately \$75,400 of contracted exam



## Findings and Recommendations

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expenses and \$788 of office insurance examiners' per diem (meals and lodging) not recorded as expenditures on the state's accounting records.

Section 33-1-413 (1), MCA, requires the insurance company examined, "shall pay the actual travel expenses, a reasonable living expense allowance, and a per diem as compensation of examiners as necessarily incurred on account of the examination, all at reasonable rates customary therefor and as established or adopted by the commissioner. . . (2) The commissioner shall pay to the state treasurer to the credit of the general fund all moneys received pursuant to subsection (1) above." In addition, section 17-1-102 (4), MCA, requires state agencies to record financial activity in order to present the receipt, use and disposition of all money for which the agency is accountable in accordance with generally accepted accounting principles. The exam expenses and reimbursements should be recorded on the state's accounting records.

Since the State Auditor's Office is required by section 33-1-401, MCA, to perform exams of domestic insurance companies, it is the office's responsibility to either perform or contract for the exams. In either case, the exams are part of the Insurance Department's operations. Office personnel said they have never recorded the expenditure and revenue activity on the state's accounting records. Personnel said they have operated under the practices described above for a number of years. They also said the office would need additional appropriation authority to record exam expenses on the state's accounting records.

As noted above, office insurance examiners' meals and lodging are billed to insurance companies, but the insurance examiners' time is not billed to the insurance companies. We believe the office examiners' time should be billed in accordance with section 33-1-413, MCA. An estimated \$3,270 could have been billed to insurance companies and deposited in the General Fund. The estimated figure is based on actual time spent at an insurance company's office. We could not quantify the additional time examiners spent working on exams while at the State Auditor's Office. When we asked why insurance examiners'

## **Findings and Recommendations**

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time is not billed, personnel said the exams are a normal duty of the office and, as such, the examiners' time is a normal expense of the office. Also, personnel said some of the smaller mutual insurance companies could not afford the exams if examiners' time was charged. However, we noted when mutual insurance companies are examined by a contract examiner, the companies are billed for the examiners' time. There is disparity in charges depending on who does the exam.

### **Recommendation #6**

**We recommend the State Auditor's Office:**

- A. Record all expenditures and revenue related to examinations of domestic insurance companies on the state's accounting records in accordance with state law.**
- B. Charge insurance companies for the time spent conducting examinations in accordance with section 33-1-413, MCA.**

### **Following Bid Requirements and Forming Written Contracts**

Selection of the contract insurance examiners is made by office personnel. There were three examiners working on five insurance examinations during the audit period. The office does not have a written contract with the examiners. We could find no evidence the scope of work, duties, period of contract, workers' compensation coverage, ownership of material, and other considerations had been specified. State policy (Management Memo 1-88-4-6) requires state agencies to sign a written contract with individuals working for an agency in a consulting or contract capacity. We also noted the office has not obtained evidence documenting if the contract insurance examiner has workers' compensation coverage, as required by state policy.

Office personnel indicated they were not aware of the state policy outlining selection and use of consultants or contracts. However, personnel did indicate they were in the process of drafting a contract to use for insurance examinations.

### Recommendation #7

We recommend the State Auditor's Office prepare written contracts for contracted services prior to the commencement of work.

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#### **Licensing Fees for Insurance Producers**

Chapter 713, Laws of 1989, made many changes to the insurance licensing laws, including changing some fee amounts. Because over 150 state laws were modified, some confusion and discrepancies occurred. Most of the changes made by Chapter 713 were effective January 1, 1990. The following report sections discuss instances where the State Auditor's Office has not implemented certain provisions of the statutes.

#### **Licensing of Nonresident Insurance Producers**

Section 33-2-708 (1) (f) (iii), MCA, requires an annual fee of \$10 for the renewal of a nonresident insurance producer license. Also, section 33-17-214, MCA, states there is an annual fee and indicates licenses will remain in effect as long as fees required in section 33-2-708, MCA, are paid. The office has not collected the annual license fee for nonresident insurance producers since the changes in laws became effective on January 1, 1990. As of February 21, 1991, there were 4,185 nonresident licenses in Montana (3,373 individual licenses and 812 agency licenses). If the fee was charged, an additional \$41,850 could be collected annually for deposit in the General Fund.

Insurance Department personnel indicated they are not charging the annual licensing fee because in the past the nonresident license has always been a perpetual license. Personnel also pointed out an inconsistency in the current law since it requires an annual renewal of license for nonresidents but not for residents. The office should require the payment of the annual renewal of nonresident licenses as required by state law. If the office believes charging the licensing fee to nonresident

## **Findings and Recommendations**

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insurance producers is not equitable, it should seek to amend sections 33-2-708 and 33-17-214, MCA.

### **Annual Renewal of Insurance Appointments**

Section 33-17-231 (3), MCA, requires the annual renewal of insurance appointments accompanied by the payment of the annual renewal fee provided by section 33-2-708, MCA. Chapter 713 eliminated the annual insurance appointment fee from section 33-2-708, MCA.

Office personnel explained the intent behind one of the changes in Chapter 713 was to increase the insurance companies' annual certificate of authority fee from \$300 to \$600 and to eliminate the annual appointment fee for insurance producers. Insurance Department personnel said the legislature intended the change in fees to be revenue neutral; the increase in the certificate of authority fee was to equal the elimination of the annual appointment fee. We noted the revenue generated by the certificate of authority fee increase was approximately equal to the decline in revenue from appointment fees in fiscal year 1989-90. To make these laws consistent, the office should seek an amendment to section 33-17-231, MCA, eliminating the provisions requiring the payment of an annual appointment fee.

### **Amendments to Insurance Producer Licenses**

The office charges \$10 for an amendment or reissuance of a resident insurance producer license. Effective January 1, 1990, Chapter 713 increased the fee for an amendment or reissuance of an original license for resident insurance producers from \$10 to \$15. Office personnel indicated they continued to charge \$10 because nonresident insurance producers still pay \$10. In the past, the fee for amendments or reissuance of an original license was the same for both residents and nonresidents. Although there is a disparity in fees charged residents and nonresidents, we believe the office should charge residents \$15 as required by section 33-2-708(1)(e)(iv), MCA. If necessary, the office should seek legislative clarification if it believes the nonresident and resident fee for amendments or reissuance of a master license should be the same.

The deputy insurance commissioner explained the office recently hired a new insurance licensing supervisor. One of the

## **Findings and Recommendations**

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supervisor's first duties will be to review all insurance licensing laws and rules in order to compile a list of all laws and rules that need to be amended to eliminate many of the issues we discovered concerning insurance producer licenses. According to office management legislative action has been requested to eliminate inconsistencies in the insurance law.

### **Recommendation #8**

**We recommend the State Auditor's Office:**

- A. Charge the fees for insurance producers as required by state law.**
- B. Seek legislation clarifying inconsistent licensing laws.**

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### **Excess Cash Balance to be Transferred to New Account**

The State Auditor's Office did not transfer the \$71,038 cash balance remaining in the firemen's pension account at the end of fiscal year 1989-90 as required by state law. Section 19-11-606, MCA, requires the state auditor to deposit any cash remaining in the firemen's pension account after the payment of claims to a new pension account established to accumulate funds for a supplemental allowance for firefighters hired on or after July 1, 1981. According to office management, the cash accumulated prior to the amendment of section 19-11-606, MCA. Office management said there is no legal requirement to transfer cash at this time because actual revenue earned by the firemen's pension account was less than expenditures paid out of the account during fiscal year 1989-90. The law requires the transfer of all remaining cash to the new account regardless of the fiscal year in which it was collected.

## **Findings and Recommendations**

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### **Recommendation #9**

**We recommend the State Auditor's Office transfer \$71,038 of remaining cash balance in the Firemen's Pension Special Revenue account to the new pension account as required by state law.**

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### **Abandoned Property**

The State Auditor's Office Insurance Department conducts regular examinations of Montana insurance companies. During the examinations, examiners identify abandoned property such as policyholders' uncashed dividend checks. The insurance examiners recommend the insurance company report the abandoned property they hold to the Montana Department of Revenue and provide the appropriate forms. However, section 70-9-314 (4), MCA, requires the State Auditor's Insurance Department to identify and report to the Montana Department of Revenue abandoned property held by insurance companies. Insurance Department personnel said they were unaware of the requirement to notify the Department of Revenue of abandoned property because the requirement is not part of the insurance laws in Title 33, MCA. Examiners could forward a copy of the letter sent to the insurance company as a means of notifying the Department of Revenue that abandoned property was found during an insurance examination.

### **Recommendation #10**

**We recommend the State Auditor's Office notify the state Department of Revenue of abandoned property held by Montana insurance companies in accordance with state law.**

# **Independent Auditor's Report & Agency Financial Schedules**

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# Summary of Independent Auditor's Report

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## Summary of Independent Auditor's Report

The auditor's opinion issued in this report is intended to convey to the reader of the financial schedules the degree of reliance that can be placed on the amounts presented.

The financial schedules are prepared from the Statewide Budgeting and Accounting System (SBAS) without adjustments for errors noted during the audit. The qualified opinion on the schedules means the reader should use caution when using the information presented. Some of the revenue is not presented in conformity with state accounting policy.



STATE OF MONTANA

Office of the Legislative Auditor

STATE CAPITOL  
HELENA, MONTANA 59620  
406/444-3122



LEGISLATIVE AUDITOR:  
SCOTT A. SEACAT

LEGAL COUNSEL:  
JOHN W. NORTHEY

INDEPENDENT AUDITOR'S REPORT

DEPUTY LEGISLATIVE AUDITORS:

MARY BRYSON  
Operations and EDP Audit  
JAMES GILLETT  
Financial-Compliance Audit  
JIM PELLEGRINI  
Performance Audit

The Legislative Audit Committee  
of the Montana State Legislature:

We have audited the accompanying financial schedules of the State Auditor's Office for each of the two fiscal years ended June 30, 1989 and 1990, as shown on pages 20 through 27. The information contained in these schedules is the responsibility of the State Auditor's Office management. Our responsibility is to express an opinion on those financial schedules based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, these financial schedules are prepared in accordance with state accounting policy and are not intended to be a presentation in conformity with generally accepted accounting principles.

The State Auditor's Office misclassified the collection of insurance premium tax as license and permits revenue in the Special Revenue Fund during fiscal year 1988-89. As a result, tax revenue was understated and license and permits were overstated by \$5,970,000 on the Schedule of Budgeted Revenue and Transfers In by Class by Fund - Estimate and Actual, for the two fiscal years ended June 30, 1990.

In our opinion, except for the matter discussed in paragraph four, the financial schedules referred to in the first paragraph present fairly in all material respects, the results of operations and changes in fund balances of the State Auditor's Office for the two fiscal years ended June 30, 1990, in conformity with the basis of accounting described in Note 1.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "James Gillett".

James Gillett, CPA  
Deputy Legislative Auditor

February 28, 1991



STATE AUDITOR'S OFFICE  
SCHEDULE OF CHANGES IN FUND BALANCES  
FOR THE TWO FISCAL YEARS ENDED JUNE 30, 1990

	<u>General Fund</u>	<u>Special Revenue Funds</u>
FUND BALANCE: July 1, 1988	\$ <u>0</u>	\$ <u>7,171,486</u>
ADDITIONS		
<u>Fiscal Year 1988-89</u>		
Budgeted Revenue and Transfers In	20,930,317	19,049,863
Prior Year Revenue Adjustments	89,812	60,832
Prior Year Transfer In Adjustments	492,155	
<u>Fiscal Year 1989-90</u>		
Budgeted Revenue and Transfers In	21,592,921	15,095,534
Direct Entries to Fund Balance	2,089,777 <sup>1</sup>	16,170
Prior Year Expenditure Adjustments		35,856
Total Additions	<u>45,194,982</u>	<u>34,258,255</u>
REDUCTIONS		
<u>Fiscal Year 1988-89</u>		
Budgeted Expenditures	975,441	16,787,015
Prior Year Expenditures	5,766	5,781
Prior Year Expenditure Adjustments	1,976	6,622,161 <sup>3</sup>
Support to State of Montana	20,529,101	
Prior Year Transfer Out Adjustments		492,155
Direct Entries to Fund Balance		2,265,812 <sup>1</sup>
<u>Fiscal Year 1989-90</u>		
Budgeted Expenditures	2,425,461	15,120,266
Prior Year Expenditure Adjustments	9,880	
Prior Year Transfer Out Adjustments	2,094,114 <sup>2</sup>	
Prior Year Revenue Adjustments	1,256,401 <sup>4</sup>	38,035
Support to State of Montana	<u>17,896,842</u>	
Total Reductions	<u>45,194,982</u>	<u>41,331,225</u>
FUND BALANCE: June 30, 1990	\$ <u>0</u>	\$ <u>98,516</u>

<sup>1</sup>See note 3.

<sup>2</sup>See note 4.

<sup>3</sup>See note 5.

<sup>4</sup>See note 6.

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules on pages 24 through 27.



STATE AUDITOR'S OFFICE  
SCHEDULE OF BUDGETED REVENUE AND TRANSFERS IN BY CLASS BY FUND - ESTIMATE & ACTUAL  
FOR THE TWO FISCAL YEARS ENDED JUNE 30, 1990

	<u>Licenses and Permits</u>	<u>Taxes</u>	<u>Fines &amp; Forfeits</u>	<u>Other Financing Sources</u>	<u>Charges For Services</u>	<u>Investment Earnings</u>	<u>Federal</u>	<u>Total</u>
<u>Fiscal Year 1989-90</u>								
GENERAL FUND								
Estimated Revenue	\$3,855,000	\$15,000,000	\$ 13,000					\$18,868,000
Actual Revenue	<u>4,190,511</u>	<u>17,296,341</u>	<u>106,069</u>					<u>21,592,921</u>
Collections Over (Under) Estimate	<u>\$ 335,511</u>	<u>\$ 2,296,341</u>	<u>\$ 93,069</u>					<u>\$ 2,724,921</u>
SPECIAL REVENUE FUND								
Estimated Revenue		\$ 6,500,000			\$401,093	\$ 80,000	\$7,000,000	\$13,981,093
Actual Revenue		<u>6,984,021</u>			<u>385,443</u>	<u>144,173</u>	<u>7,581,897</u>	<u>15,095,534</u>
Collections Over (Under) Estimate		<u>\$ 484,021</u>			<u>\$(15,650)</u>	<u>\$ 64,173</u>	<u>\$ 581,897</u>	<u>\$ 1,114,441</u>
<u>Fiscal Year 1988-89</u>								
GENERAL FUND								
Estimated Revenue	\$ 775,000	\$20,348,000	\$21,500	\$ 2,233,000 <sup>1</sup>				\$23,377,500
Actual Revenue	<u>764,650</u>	<u>20,118,164</u>	<u>47,503</u>	<u>0</u>				<u>20,930,317</u>
Collections Over (Under) Estimate	<u>\$ (10,350)</u>	<u>\$ (229,836)</u>	<u>\$26,003</u>	<u>\$(2,233,000)</u>				<u>\$(2,447,183)</u>
SPECIAL REVENUE FUND								
Estimated Revenue	\$9,014,000 <sup>2</sup>	\$ 1,000,000			\$385,700	\$ 55,000	\$6,000,000	\$16,454,700
Actual Revenue	<u>9,325,601</u>	<u>960,402</u>			<u>378,003</u>	<u>147,312</u>	<u>8,238,545</u>	<u>19,049,863</u>
Collections Over (Under) Estimate	<u>\$ 311,601</u>	<u>\$ (39,598)</u>			<u>\$ (7,697)</u>	<u>\$ 92,312</u>	<u>\$2,238,545</u>	<u>\$ 2,595,163</u>

<sup>1</sup>See note 4.

<sup>2</sup>See note 7.

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules on pages 24 through 27.



STATE AUDITOR'S OFFICE  
SCHEDULE OF BUDGETED PROGRAM EXPENDITURES BY OBJECT AND FUND - BUDGET AND ACTUAL  
FOR THE FISCAL YEAR ENDED JUNE 30, 1990

	Central Administration	State Payroll	Insurance	Securities	Local Assistance Distribution	Forest Res & FPGA To Counties	Pension Adj Retired Firemen	Fiscal Control & Management	Total
PERSONAL SERVICES									
Salaries	\$168,498	\$191,702	\$537,460	\$191,806				\$162,569	\$ 1,252,035
Employee Benefits	38,390	42,965	118,275	41,816				38,119	279,565
Total	<u>206,888</u>	<u>234,667</u>	<u>655,735</u>	<u>233,622</u>				<u>200,688</u>	<u>1,531,600</u>
OPERATING EXPENSES									
Other Services	2,598	532,766	24,264	10,281				163,325	733,234
Supplies & Materials	3,307	12,158	19,946	9,964				36,635	82,010
Communications	4,896	12,592	40,307	10,532				160,918	229,245
Travel	1,925	1,568	36,120	6,627				332	46,572
Rent	1,662	15,166	15,176	2,701				15,166	49,871
Repair & Maintenance	1,753	4,183	9,735	4,014				18,196	37,881
Other Expenses	2,747	2,399	5,275	1,923				6,351	18,695
Total	<u>18,888</u>	<u>580,832</u>	<u>150,823</u>	<u>46,042</u>				<u>400,923</u>	<u>1,197,508</u>
EQUIPMENT AND INTANGIBLE ASSETS									
Equipment	102	11,979	572	36,520				33,383	82,556
Total	<u>102</u>	<u>11,979</u>	<u>572</u>	<u>36,520</u>				<u>33,383</u>	<u>82,556</u>
LOCAL ASSISTANCE									
From Federal Sources						\$7,715,901			\$ 7,715,901
From Other Income Sources					\$6,075,672		\$ 942,490		7,018,162
Total					<u>6,075,672</u>	<u>7,715,901</u>	<u>942,490</u>		<u>14,734,063</u>
TOTAL PROGRAM EXPENDITURES	<u>\$225,878</u>	<u>\$827,478</u>	<u>\$807,130</u>	<u>\$316,184</u>	<u>\$6,075,672</u>	<u>\$7,715,901</u>	<u>\$ 942,490</u>	<u>\$634,994</u>	<u>\$17,545,727</u>
GENERAL FUND									
Budgeted	\$232,389	\$448,570	\$969,908	\$323,728				\$657,234	\$ 2,631,829
Actual	<u>225,878</u>	<u>441,275</u>	<u>807,130</u>	<u>316,184</u>				<u>634,994</u>	<u>2,425,461</u>
Unspent Budget Authority	<u>\$ 6,511</u>	<u>\$ 7,295</u>	<u>\$162,778</u>	<u>\$ 7,544</u>				<u>\$ 22,240</u>	<u>\$ 206,368</u>
SPECIAL REVENUE FUND									
Budgeted		\$406,609			\$6,100,000	\$7,715,901	\$1,000,000		\$15,222,510
Actual		<u>386,203</u>			<u>6,075,672</u>	<u>7,715,901</u>	<u>942,490</u>		<u>15,120,266</u>
Unspent Budget Authority		<u>\$ 20,406</u>			<u>\$ 24,328</u>	<u>\$ 0</u>	<u>\$ 57,510</u>		<u>\$ 102,244</u>

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules on pages 24 through 27.





STATE AUDITOR'S OFFICE  
SCHEDULE OF BUDGETED PROGRAM EXPENDITURES BY OBJECT AND FUND - BUDGET AND ACTUAL  
FOR THE FISCAL YEAR ENDED JUNE 30, 1989

	Central Administration	Audit <sup>1</sup> Division	Insurance	Securities	Local Assistance Distribution	Forest Res & FPGA to Counties	Pension Adj Retired Firemen	Total
PERSONAL SERVICES								
Salaries	\$163,420	\$ 342,961	\$ 466,396	\$ 190,281				\$ 1,163,058
Other Compensation		50						50
Employee Benefits	<u>37,548</u>	<u>78,190</u>	<u>104,543</u>	<u>41,013</u>				<u>261,294</u>
Total	<u>200,968</u>	<u>421,201</u>	<u>570,939</u>	<u>231,294</u>				<u>1,424,402</u>
OPERATING EXPENSES								
Contracted Services	5,428	481,180	48,689	8,774				544,071
Supplies & Materials	4,346	26,979	12,647	12,010				55,982
Communications	22,700	77,791	108,917	8,884				218,292
Travel	129	2,182	28,233	9,573				40,117
Rent	2,358	29,122	15,274	2,432				49,186
Repair & Maintenance	1,079	14,100	3,106	5,000				23,285
Other Expenses	<u>2,709</u>	<u>2,083</u>	<u>6,318</u>	<u>2,838</u>				<u>13,948</u>
Total	<u>38,749</u>	<u>633,437</u>	<u>223,184</u>	<u>49,511</u>				<u>944,881</u>
EQUIPMENT AND INTANGIBLE ASSETS								
Equipment		<u>95,376</u>	<u>9,948</u>					<u>105,324</u>
Total		<u>95,376</u>	<u>9,948</u>					<u>105,324</u>
LOCAL ASSISTANCE								
From Federal Sources						\$8,385,856		8,385,856
From Other Income Sources					<u>\$5,967,821</u>		<u>\$ 934,172</u>	<u>6,901,993</u>
Total					<u>5,967,821</u>	<u>8,385,856</u>	<u>934,172</u>	<u>15,287,849</u>
TOTAL PROGRAM EXPENDITURES	<u>\$239,717</u>	<u>\$1,150,014</u>	<u>\$ 804,071</u>	<u>\$ 280,805</u>	<u>\$5,967,821</u>	<u>\$8,385,856</u>	<u>\$ 934,172</u>	<u>\$17,762,456</u>
GENERAL FUND								
Budgeted	\$240,749	\$ 751,633						\$ 992,382
Actual	<u>239,717</u>	<u>735,724</u>						<u>975,441</u>
Unspent Budget Authority	<u>\$ 1,032</u>	<u>\$ 15,909</u>						<u>\$ 16,941</u>
SPECIAL REVENUE FUND								
Budgeted		\$ 433,187	\$1,244,442	\$2,101,251	\$5,970,000	\$8,386,000	\$1,000,000	\$19,134,880
Actual		<u>414,290</u>	<u>804,071</u>	<u>280,805</u>	<u>5,967,821</u>	<u>8,385,856</u>	<u>934,172</u>	<u>16,787,015</u>
Unspent Budget Authority		<u>\$ 18,897</u>	<u>\$ 440,371</u> <sup>2</sup>	<u>\$1,820,446</u> <sup>2</sup>	<u>\$ 2,179</u>	<u>\$ 144</u>	<u>\$ 65,828</u>	<u>\$ 2,347,865</u>

<sup>1</sup>See note 7.

<sup>2</sup>See note 4.

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules on pages 24 through 27.



# Notes to Financial Schedules

## For the Two Fiscal Years Ended June 30, 1990

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### 1. Summary of Significant Accounting Policies

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#### Basis of Accounting

The State Auditor's Office uses the modified accrual basis of accounting, as defined by generally accepted accounting principles, for its Governmental Funds. In applying the modified accrual basis, the office records:

Revenues when it receives cash or when receipts are measurable and available to pay current period liabilities.

Expenditures for valid obligations when the office incurs the related liability and it is measurable.

The following additional items may be considered valid obligations or expenditures under state accounting policy:

- The entire budgeted service contract even though the office received the services in a subsequent fiscal year.
- Goods ordered with a purchase order before fiscal year-end, but not received as of fiscal year-end.
- Equipment ordered with a purchase order before fiscal year-end.

State accounting policy also requires the office to record the cost of employees' annual leave and sick leave when used or paid.

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#### Basis of Presentation

The financial schedules are prepared from the Statewide Budgeting and Accounting System (SBAS) without adjustment. Accounts are organized in funds according to state law. The office uses the following funds:

#### Governmental Funds

**General Fund** - to account for all financial resources except those required to be accounted for in another fund. The office's Central Administration, Insurance, Securities, and Fiscal Management and Control programs are funded by the General Fund in fiscal year 1989-90. The major source of revenue for the General Fund is insurance premium taxes.

## Notes to Financial Schedules

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**Special Revenue Fund** - to account for proceeds of specific revenue sources legally restricted to expenditures for specific purposes. Office Special Revenue Funds include accounts for police and fire retirement/pension payments and central payroll operations. During fiscal year 1988-89 the Special Revenue Fund also accounted for the Insurance and Securities Regulatory Trust accounts.

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### 2. General Fund Balance

The General Fund is a statewide fund. Agencies do not have a separate General Fund since their only authority is to pay obligations from the statewide General Fund within their appropriation limits. Thus, on an agency's schedules, the General Fund beginning and ending fund balance will always be zero.

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### 3. Direct Entry to Fund Balance

The direct entries to fund balance in the Special Revenue Fund and General Fund for fiscal years 1988-89 and 1989-90 consist of transactions processed to clear out the Insurance and Securities Regulatory Trust accounts. Senate Bill 78, Laws of 1989, eliminated the Insurance and Securities accounts from the state Special Revenue Fund.

The Department of Administration, Accounting Bureau, processed transactions to clear out the Insurance and Securities Regulatory Trust Account fund balances at the end of fiscal year 1988-89. This results in the \$2,265,812 direct entry to fund balance in the Special Revenue Fund for fiscal year 1988-89. The State Auditor's Office restored the fund balances in the regulatory accounts during fiscal year 1989-90 in order to complete transactions prior to the final closing out of the regulatory accounts. Final closing transactions results in the General Fund direct entry to fund balance of \$2,089,777 for fiscal year 1989-90.

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**4. Transfers**

During fiscal year 1988-89, state law required the cash balance remaining in the Securities and Insurance Regulatory Trust accounts be transferred to the General Fund. The office established transfer appropriations from the trust accounts to the General Fund. Rather than transferring the cash balance for the regulatory accounts, a direct entry to fund balance was processed as explained in Note 3. Because of this, the Schedule of Budgeted Revenue and Transfers In for the General Fund shows an estimated transfer in revenue of \$2,233,000 and actual revenue of \$0 for the revenue classification of Other Financing Sources and the Special Revenue Fund expenditure authority of \$440,371 and \$1,820,446 remained in the Insurance and Securities programs, respectively, on the Schedule of Budgeted Program Expenditures by Object and Fund for fiscal year 1988-89.

During fiscal year 1989-90, the office processed transactions to record the fiscal year 1988-89 transfers of Insurance and Security Regulatory Trust accounts which, when combined with the transactions to close the regulatory accounts, result in a \$2,094,114 prior year transfer out adjustment in the General Fund on the Schedule of Changes in Fund Balances.

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**5. Prior Year Expenditure Adjustments**

During fiscal year 1988-89, the office recorded the fiscal year 1987-88 payments to the Public Employees' Retirement Division and local cities and towns for various police and firemen retirement accounts. The payments were not recorded on the state's accounting records during fiscal year 1987-88. Therefore, \$6,622,161 was recorded as prior year expenditures in fiscal year 1988-89 in the Special Revenue Fund.

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**6. Prior Year Revenue Adjustments**

The prior year revenue adjustments of \$1,256,401 in the General Fund relate to refunds of fiscal year 1988-89 insurance tax premiums. The majority relates to one insurance company which overpaid on two of its quarterly tax payments during fiscal year 1988-89. The company subsequently discovered an error in its calculation of the tax and requested a refund for the overpayments. The refund was made during fiscal year 1989-90 as a prior year revenue adjustment.

## Notes to Financial Schedules

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### 7. Reorganization

The Insurance and Securities Regulatory Trust Special Revenue Fund accounts were eliminated beginning in fiscal year 1989-90. The License and Permits revenue activity associated with the regulatory accounts in the Special Revenue Fund for fiscal year 1988-89 was eliminated and the revenue is reflected in the License and Permits and Taxes categories in the General Fund for fiscal year 1989-90. A portion of insurance premium taxes used to provide for the state's contributions to the police and firefighter's retirement systems was misclassified as License and Permits revenue during fiscal year 1988-89. All insurance premium taxes are classified as taxes in fiscal year 1989-90 in the General and Special Revenue Funds. The Schedule of Budgeted Program Expenditures for fiscal year 1988-89 shows financial activity of the Audit Division. This division was split into the State Payroll and Fiscal Control and Management Divisions in fiscal year 1989-90.

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### 8. Annual and Sick Leave

Employees at the office accumulate both annual and sick leave. The office pays employees for 100 percent of unused annual and 25 percent of unused sick leave credits upon termination. Accumulated unpaid liabilities for annual and sick leave are not reflected in accompanying financial schedules. The office absorbs expenditures for termination pay in its annual operational costs. The office had a liability for annual and sick leave of \$93,198 at June 30, 1989 and \$117,126 at June 30, 1990.

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### 9. Pension Plan

Employees are covered by the Montana Public Employees' Retirement System (PERS). The office's contribution to PERS was \$73,912 in fiscal year 1988-89 and \$79,147 in fiscal year 1989-90.

## Agency Response

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STATE AUDITOR  
STATE OF MONTANA



Andrea "Andy" Bennett  
STATE AUDITOR

COMMISSIONER OF INSURANCE  
COMMISSIONER OF SECURITIES

APR 26 1991

April 25, 1991

Scott A. Seacat  
Legislative Auditor  
State Capitol  
Helena, MT 59620

Dear Mr. Seacat:

The State Auditor's Office response to the recommendations in the Financial Compliance Audit for the two fiscal years ended June 30, 1990, is attached.

With best personal regards, I am

Very truly yours,

A handwritten signature in cursive script, appearing to read "Andy Bennett".

Andrea "Andy" Bennett  
State Auditor

AB/dse(724)  
Attach.

## AUDIT RECOMMENDATIONS

### Recommendation #1

We recommend the State Auditor's Office comply with the provisions of its appropriation laws.

We concur with this recommendation.

### Recommendation #2

We recommend the State Auditor's Office comply with the personal service restrictions in the appropriation law.

We partially concur. Although individual time sheets do not reflect detail, it is common for Central Administration and mail and delivery services to provide support to other departments. This support is not on an hour to hour basis, but includes personnel and financial support. The State Auditor's Office has completed a reorganization of the payroll and warrant writing systems to accurately reflect duties. Also, the State Auditor has requested additional funds from the Legislature during the last two sessions to adequately compensate Central Administration staff. We will record the proper departments on time rolls, however, there was no transfer of funds between programs.

### Recommendation #3

We recommend the State Auditor's Office:

- A. Accrue only valid obligations as defined by state law.
- B. Revert \$24,780 of appropriation authority to the General Fund.

Part A - We concur with this recommendation.

Part B - We do not concur with this recommendation.

The State Auditor's Office accrued this funding based on correspondence with the Office of Budget and Program Planning and the Information Services Division of the Department of Administration.

The correspondence and work orders from ISD were done well in advance of fiscal year-end. The inter-agency agreement was not signed until August 20, 1990. This office felt that the documentation and correspondence accurately

detailed the purpose and content of the accrual. Based on the documentation and the fact that these funds are being used as specified in the original appropriation, and as documented several times, there is no cause or justification for a reversion of funds.

#### Recommendation #4

We recommend the State Auditor's Office record revenue in the general fund for money received from the sale of copies and documents.

We concur - The State Auditor's Office will seek appropriation authority from the legislature in order to expense outside copying costs rather than abate the expenditure. We have not requested spending authority in the past due to the fact these charges are public services outside the regular office operation and not predictable.

#### Recommendation #5

We recommend the State Auditor's Office:

- A. Establish procedures to ensure the accuracy of payments to the Public Employees' Retirement Division prior to making payments.
- B. Work with the Public Employees' Retirement Division to determine the amount of money owed for late pension payments.

Part A - We concur with this part of the recommendation. The State Auditor's Office has already implemented document review procedures to ensure the accuracy of all payments made to the Public Employees' Retirement Division.

Part B - We concur with this part of the recommendation. We agree that the pension system did lose approximately \$67,610 in interest earnings due to the late payments made by the State Auditor's Office in fiscal year 1989. However, the pension system gained approximately \$66,803 in interest earnings due to early payments made by the State Auditor's Office in fiscal year 1990. Therefore, we do not agree with the information contained in the body of this audit report which implies that the State Auditor's Office should return \$67,610 in lost pension system interest to the Public Employees' Retirement Division. We plan to work with the Public Employees' Retirement Division to determine the amount of money owed for late pension payments.

## Recommendation #6

We recommend the State Auditor's Office:

- A. Record all expenditures and revenue related to examinations of domestic insurance companies on the state's accounting records in accordance with state law.
- B. Charge insurance companies for the time spent conducting examinations in accordance with Section 33-1-413, MCA.

Part A - We do not concur with this part of the recommendation. Most examinations are performed by contract examiners. Contracted examiners meet qualification standards established by the National Association of Insurance Commissioners (NAIC). Examiners are assigned according to NAIC guidelines. The office does not supervise the activities of the contract examiner, but rather reviews the work product for compliance with statutory and National Association of Insurance Commissioner standards. The office assures that examiners are qualified and independent of the subject company, and that the report fairly states the condition of the subject. The environment of the Department is no greater than that.

The contracted examiners are independent contractors of the subject company. Contracted examiners are not employees of the Office of the State Auditor. The submission by an insurer to examination is a necessary condition to maintain a certificate of authority, just as the maintenance of minimum surplus is. It is fairer to say that the work of examiners is part of the operations of the insurer than the Office of the State Auditor.

The current system is analogous to the way the Local Government Services Bureau of the Department of Commerce causes audit examinations of political subdivisions of the State of Montana. There, when the audits are contracted to independent CPA firms, the auditors are paid directly by the subjects. The same applies here.

Part B - We do not concur with the part of the recommendation.

Staff examiners, when hired, typically have a bachelor's degree in accounting and no experience or background in statutory accounting principles. A major responsibility of the Examiner's Division is to review the annual reports of all insurers authorized to do business in Montana. These are prepared in accordance with statutory accounting principles. To assist the

subordinate examiners to become knowledgeable about statutory accounting principles, the Administrator, from time to time, assigns staff examiners to conduct the examination of a domestic insurer. Unlike the examinations done by contract examiners, these are done under the close supervision of the administrator of the Examinations Division.

Because these examinations have a training purpose, the office believes that it is inappropriate to charge the subject companies for the time of its examiners. The time is a normal expense, just as time spent by the examiners to attend educational seminars is.

The office has established a procedure whereby the office alternates on successive examinations the use of contract examiners with the use of employed examiners. Once the course of examination cycles, the costs of examination of each insurer will even out.

#### Recommendation #7

We recommend the State Auditor's Office prepare written contracts for contracted services prior to the commencement of work.

We concur with this recommendation.

#### Recommendation #8

We recommend the State Auditor's Office:

- A. Charge the fees for insurance producers as required by law.
- B. Seek legislation clarifying inconsistent licensing laws.

Part A - We concur with this recommendation.

Part B - We concur with this recommendation.

#### Recommendation #9

We recommend the State Auditor's Office transfer \$71,038 of remaining cash balance in the Firemen's Pension Special Revenue account to the new pension account as required by state law.

We do not concur with this recommendation. The \$71,038 of remaining cash balance in the Firemen's Pension Special Revenue account is excess funds built-up from fiscal years

prior to the amendment of 19-11-606, MCA (the amendment requires the transfer of excess cash to the new account). We feel the amendment to 19-11-606, MCA, which was effective beginning in fiscal year 1990 intended for a transfer to be made if tax collections resulted in excess cash collected during fiscal year 1990 and thereafter. However, tax collections in fiscal year 1990 resulted in a deficit situation. In other words, actual revenue from the Firemen's Pension Tax in fiscal year 1990 was insufficient to pay supplemental retirement benefits due pursuant to 19-13-1006, MCA. The deficit was made up by using the pre-1990 excess to pay the retirement benefits due retirees. We intend to fully comply with the law requiring the transfer of excess cash if, and when, excess cash is collected during present and future fiscal years. Until then, we plan to use the pre-1990 excess cash to invest in the state's Short Term Investment Pool and supplement current-year collections in order to fully pay the retirement benefits due retirees. We feel it is important to note that revenue shortfalls are expected in the Firemen's Pension Special Revenue account for at least the next several years. We feel that the intent of the amendment to 19-11-606, MCA, was to benefit future retired firefighters, but not at the expense of older retirees who have benefited from the Firemen's Pension Tax for many years.

#### Recommendation #10

We recommend the State Auditor's Office notify the State Department of Revenue of abandoned property held by Montana insurance companies in accordance with state law.

We concur with this recommendation.

JDS/flo(723)



